

448

# The Merchants' Association of New York



- I: OPPOSING GOVERNMENT OWNERSHIP AND OPERATION OF PUBLIC UTILITIES.
- II: ADVOCATING EXCLUSIVE REGULATION OF ALL RAILROADS BY THE FEDERAL GOVERNMENT.

SUPPLEMENT NO. 33.  
FOR  
BRIEF OF ARGUMENTS  
AGAINST  
PUBLIC OWNERSHIP.

November, 1916



# The Merchants' Association of New York



- I: OPPOSING GOVERNMENT OWNERSHIP AND OPERATION OF PUBLIC UTILITIES.
- II: ADVOCATING EXCLUSIVE REGULATION OF ALL RAILROADS BY THE FEDERAL GOVERNMENT.

November, 1916

THE Merchants' Association of New York, on the recommendation of its Committee on Transportation, has adopted the following preambles and resolutions:

- I: Opposing government ownership and operation of public utilities;
- II: Advocating the exclusive regulation of all railroads by the Federal Government;

has approved the appended arguments prepared under the direction of the Committee; and directed that the Association, through its representatives, appear before the Newlands Commission in support thereof.

New York, November 15, 1916.

S. C. MEAD,  
*Secretary.*

## I: RESOLUTIONS.

---

### I:—OPPOSING GOVERNMENT OWNERSHIP AND OPERATION OF PUBLIC UTILITIES.

*Whereas*, The Newlands Commission, created by Senate Joint Resolution No. 60, is about to investigate, among other things, “the comparative worth and efficiency of governmental regulation and control [of public utilities] as compared with governmental ownership and operation” and

*Whereas*, The fundamental principles of our form of government require;

That the members of legislative bodies and all principal executive officials be periodically subject to change;

That the number of members of legislative bodies be large and that representation be sectional;

That legislative bodies, by means of laws passed by them, direct and control in minute detail the acts of executive officials;

That the discretionary power of such officials be restricted to the narrowest possible limits;

That no outlays of public monies be made except as expressly authorized by law; and

*Whereas*, By reason of these conditions inseparable from our form of government, governmental operation of eco-

nomic undertakings, whether Federal, State or Municipal, is characterized by :

Extreme delay and inertia, vacillation, hesitancy and inconsistency in matters of policy;

Wasteful outlays in response to sectional demands;

Insufficient provision of funds when needed for necessary purposes;

Absence of close and harmonious co-operation between the legislative directorate and the executive officials;

Insecurity of tenure in the higher places and lack of self-interest as an incentive;

Frequent change of higher officials and the injection into office of new and untried men;

Unsuitable methods of selecting executive officials whereby such officials are often not properly qualified by expert knowledge, previous training, experience or proved capacity;

Hampering conditions imposed by law upon executives whereby they are deprived of necessary control of operation and of their subordinates; and

*Whereas*, From these conditions naturally result imperfect co-ordination, lack of qualified management, bad operating methods, and general waste and inefficiency; both the methods and the results being diametrically opposite to those which prevail in properly managed business undertakings, which latter are governed solely by economic considerations, and require for their success close and friendly relations between the directorate and the officials; the prompt provision of funds as required by the economic needs of the business; high capacity, long ex-

perience and special training on the part of the executive officials, assured tenure during efficiency, self-interest, and the possession by such officials of a very large degree of discretion as to outlays and operating details; Now, therefore, be it

*Resolved*, By The Merchants' Association of New York that governmental methods in the conduct of business affairs are inherently defective by reason of the fundamental restrictions imposed by our form of government; and that governmental methods are often inefficient and wasteful and therefore unsuited to the conduct of business undertakings; And be it further

*Resolved*, That The Merchants' Association of New York is opposed to government ownership and operation of railroads, telephones, telegraphs, and other public utilities, believing that such utilities are far more effectively operated under private ownership, subject to public regulation, than would be possible under governmental ownership and operation, and that it would be a national calamity to subject these instruments, indispensable to the welfare of the whole country to the hampering, inefficient and wasteful methods inseparable from governmental undertakings.

## **II:—ADVOCATING THE EXCLUSIVE REGULATION OF ALL RAILROADS BY THE FEDERAL GOVERNMENT.**

*Whereas*, It is vital to the welfare of the whole country that the entire system of railroads of the nation be maintained

upon a level of the highest efficiency, to which end regulation by public authority is necessary ; and

*Whercas*, The railroads of the country are now subject to regulation by the Federal government and by each of the forty-eight states, which multiple control by independent authorities results in a large body of unrelated, unco-ordinated and, often conflicting legislation ; in the enactment by some states of regulatory laws which interfere with the rights or laws of other states ; in requirements as to equipment, methods and conditions of operation, differing in the several states, with which compliance is difficult and sometimes impossible ; in the fixing by different states of different rates of charge for a similar or identical service ; in great increase in the cost of operation and in making difficult the conduct of a railroad operating in two or more states ; and

*Whercas*, Nineteen different states now prescribe the conditions under which securities may be issued by railroads operating within their borders, nearly every railroad thereby being subject, in the matter of issuance of securities, to the requirements of two or more states, each having power to refuse its assent and thereby to prevent the issuance of such securities, and to require the expenditure within its own borders of part of the proceeds of such securities, irrespective of the place where the expenditure is properly required ; and

*Whercas*, The effect of this multiple regulation has greatly and wastefully increased the outlays of the railroads without increasing their earning power, and has curtailed their revenues by direct reduction of rates ; and

*Whereas*, By reason of these causes among others, the credit of the railroads has been gravely impaired within recent years, through the insufficiency of earnings and the unwillingness of the public to invest its capital subject to hostile attacks by numerous legislative bodies, so that there exists a condition under which new issues of railroad stocks offer little attraction to permanent investors, the sole source of additional financial support available to railroads being the issuance of bonds secured by mortgages upon the property, which resource is rapidly becoming unavailable by reason of the existence of prior liens; Now, therefore, Be it

*Resolved*, By the Merchants' Association of New York that the welfare of the nation requires that the railroads of the country be maintained on the highest practicable plane of efficiency; that multiple control by diverse state authorities, as well as by Federal authority, has become undesirable and harmful, that while the public interest requires that all the railroads of the country shall be effectively regulated in the public interest, such regulation can best be effected by the sole authority of the Federal government, thereby insuring consistency and uniformity of regulation, and consideration of the economic necessity of so protecting the revenues of the railroads as to enable them to attain and maintain the efficiency demanded in the public service;

*Resolved*, That if Congress already possesses the necessary Constitutional power to effect such sole regulation by Federal authority, it is urged that Congress fully assert and exercise that power forthwith; or, if the present

powers of Congress appear insufficient for that purpose, that the necessary powers should be provided by amendment of the Constitution.

*Resolved*, That such regulation should include sole control by the Federal government of the conditions under which railroad securities may be issued, and that as means to that end, Federal incorporation of railroads be provided for;

*Resolved*, That the Interstate Commerce Commission should be so enlarged and its procedure so arranged as to enable it effectively and promptly to despatch the business imposed upon it.

## II: CONDITIONS WHICH PRECLUDE EFFICIENCY AND ECONOMY IN GOVERNMENTAL OPERATION OF PUBLIC UTILITIES.

---

### I.—THE FUNDAMENTALS OF ECONOMIC EFFICIENCY.

1:—The fundamental assumption which underlies the argument for Governmental ownership and operation of public utilities is that a profit equal to that now secured by private corporations through private operation can be secured for the public benefit by public operation; or that, as an alternative, by the elimination of profit, service may be increased or charges reduced.

2:—This implies that public management will be as economically efficient and productive as private or corporate management. The latter assumption is unwarranted. On the contrary, it can be shown that Governmental management is fundamentally defective in important particulars; that its defects are inherent in and inseparable from our system of Government; and that those defects make relative inefficiency and uneconomy inevitable.

3:—The Governmental methods adapted to and in many respects admirable for the primary purposes of Government; namely, the protection of life, property and civil rights, are unadapted to the successful management of industrial undertakings, in which economic, as distinguished from political, principles must be regarded.

Fundamental principles of our system of government are that the personnel of the legislative and the higher officials of the executive branches be subject to periodical change ; that executive discretion be closely limited by law ; and that no outlays of public monies be made except expressly authorized by law. We have here the assurance of frequent changes in both directive and administrative control ; the practical certainty of frequent and perhaps radical changes of policy ; the impairment of executive efficiency ; and the delay or withholding of necessary funds. These conditions which are of political origin and are inescapable make economic efficiency impossible.

4 :—Economic efficiency requires the incentive of self-interest, not only on the part of the owners of a business enterprise, but also on the part of all employees ; a definite, carefully planned, and consistent policy ; a perfectly co-ordinated plan of operation ; prompt provision of funds needed for plant betterments and extensions ; constant and intimate touch between directorate and executive ; infrequent change of executive officials, tenure during efficiency, and practically unrestricted executive authority over operation. All these requisites are present in well-managed industrial corporations ; most of them are usually, and some of them are always, lacking in public undertakings.

5 :—The fundamental defects of Governmental operation, nearly always present, are :

- (a) Dilatory, inconsistent, vacillating and therefore ineffective and wasteful policy.
- (b) Unsuitable, inefficient and frequently changed executive organization.
- (c) Hampering limitations upon executives.

- (d) Lack of self-interest as an incentive.
- (e) Lack of standards of efficiency.

6:—In all business operations, the following conditions are requisite to economic efficiency:

#### THE DIRECTORATE:

The essentials of an efficient directorate are:

General business capacity and experience; special knowledge of the particular business; financial interest;

Intimate and continuous contact with the affairs under their direction;

Close, constant and harmonious relations between the directorate and the executive;

Prompt action upon the executive's recommendations and upon all questions of policy whenever they arise.

#### THE EXECUTIVE:

The essentials of an efficient executive are:

Comprehensive experience, and thorough special training; exceptional organizing and executive ability; and intimate knowledge of detail;

Full accord with the directorate as to policy and a considerable degree of influence in determining policy;

Practically complete control over organization, personnel, operating methods, and all details. Full enlistment of self-interest as an incentive.

7:—Practically every important business corporation having to do with physical operations conforms to these requirements.

The members of the Board of Directors of such a corporation are usually chosen because of their general business experience, sagacity and sound judgment; their intimate knowledge of the business undertaken; and their personal financial interest in its profitable management.

8:—In the management of economic affairs, important questions of policy are constantly arising. Unless promptly and wisely disposed of, the business is embarrassed, hampering and wasteful conditions arise or continue, and the business becomes unprofitable. Hence, capable business boards meet at short intervals, promptly consider and dispose of the questions of policy submitted by the management, vote the funds needed to secure or maintain economic efficiency, and in general make the authorizations which the executive demonstrates are necessary to the welfare of the business.

9:—A business board will select an executive of proved ability, a man in whose sound judgment they have confidence, will give him prompt and ample support, allow him wide discretion as to methods and means, and hold him to full responsibility for results. Thus the executive is enabled promptly to do what needs to be done to make the business economically successful. His full ability, zeal and energy are enlisted to promote efficiency, prevent waste and earn profits.

10:—Contrary conditions govern the direction and management of all Governmental undertakings. The Federal Government may be used for purposes of illustration.

## **II.—DEFECTS OF CONGRESS AS A DIRECTORATE.**

11:—It is axiomatic in business affairs that large directorates are not adapted to the prompt despatch of business,

to judicious outlay or to economy of operation. Congress, which has 531 members is, in effect, the Board of Directors of whatever business enterprise the Government undertakes. It determines by law what shall be done; it prescribes by law, often in minute detail, the manner in which it shall be done; it jealously restricts the power of the executive; it gives or withholds funds and dictates minutely the manner in which they shall be applied, thereby controlling in detail, the methods and the operations of the executive branch.

#### INERTIA AND ITS EVIL RESULTS.

12:—A Board of Directors comprising 531 members is inevitably extremely slow in its operation. Every question involves great divergence of views and a wide range of conflicting interests. Political expediency, partisan and sectional demands, conflicting economic theories, personal motives, selfish influences, and popular clamor are inseparable factors. From the play of these opposing forces results prolonged inertia, frequently protracted for years; and strictly economic questions, when finally decided, are seldom decided solely upon economic considerations. Practically every decision is a compromise, which frequently discards some essentials and includes mischievous riders and often paralyzing restrictions.

While such delay may not be serious in political matters, it is deadly to economic enterprises in which prompt determination of policy is frequently vital, and always requisite to efficiency and economy of management.

#### EMBARRASSMENT OF EXECUTIVE ARISING FROM INERTIA OF DIRECTORATE:

13:—No executive, however able and zealous, can administer any business economically or with reasonable efficiency,

when authorizations, without which immediately necessary operations cannot be undertaken, are delayed for months or years. Executive recommendations of a nature requiring prompt action are by Congress commonly delayed indefinitely, frequently refused or ignored. In consequence an important function is badly and wastefully performed, an inefficient organization continued at excessive cost, or a pressingly needed and partially completed public work delayed, with material increase in cost as a result.

#### WASTE CAUSED BY DELAYED APPROPRIATIONS.

14:—The failure or refusal of Congress to grant appropriations for construction as required for the most economical prosecution of the work is the cause of great waste. Nearly all extensive Federal works are financed on the basis of assumed successive annual appropriations. But in many instances the appropriations necessary to uninterrupted work are not made and the work is suspended. This causes excessive delay in completion and largely increased cost. It commonly requires years to erect a public building, where private enterprise would finish a similar building within a much shorter time. Contractors always consider the element of delay and the large increase in cost consequent thereon, and contract prices for public works dependent upon successive annual appropriations are always materially greater than in the case of private works. Moreover, where the construction period is unduly protracted there are large and wasteful outlays for interest charges and administration expenses, and loss by deterioration of plant.

#### BAD EFFECT OF PERIODIC CHANGES IN CONGRESS.

15:—The personnel of Congress changes to a consider-

able degree every two years. The political complexion of one or both houses changes at uncertain intervals. The President, who has power to nullify what Congress adopts, is sometimes antagonistic to the purposes of Congress. Many or all the experienced members of important committees are occasionally displaced and substituted by new members without adequate knowledge of the affairs largely subject to their control. The tendency to inertia from the causes recited in a previous paragraph is greatly increased by these periodic changes; and in the event of a complete change or a division of party control, a modification or reversal of policy as to projects previously authorized is also very likely.

16:—An incoming party always criticises the acts, and particularly the expenditures of the party formerly in power, and occasionally undoes the acts, or withholds support from the projects of the latter. Hence, results an inconsistent, halting and vacillating policy, with consequent disruption of well-conceived and excellent plans previously authorized but still in the formative stages; the suspension of work upon construction already begun; the occasional modification or partial change of physical plans, and the abandonment of physical works which have cost considerable sums.

17:—These conditions of vacillating or hesitant policy, are destructive of executive efficiency, as they retard or prevent the provision of essential and often urgently needed structures or plant, and make well co-ordinated and economical operation impossible.

In few words, the results of vacillating policy are intermittent or inadequate financial support, patchwork planning, piece-meal construction, inadequate plant, makeshift operation and excessive cost.

## INFLUENCE OF SECTIONAL DEMANDS:

18:—It is inevitable that the action of Congress as to physical undertakings involving large outlays is greatly swayed by sectional demands; and seldom indeed is Congressional decision as to purely economic projects based solely upon economic utility. The proposition that expenditures for public improvements should be territorially distributed is plausible and popular, however economically unsound. The pressure of their constituents forces most Congressmen to support that proposition, whatever their private view may be. Hence a wide demand for local improvements to which Congress must necessarily give consideration.

19:—Unless concession be made to these demands a hostile combination will prevent the passage of an entire appropriation bill, and thus defeat many projects which are perhaps urgently necessary. In the case of public buildings and river and harbor improvements the sectional demands are co-extensive with the National territory; and in perhaps the majority of cases have little economic justification. A handsome Federal building costing several hundred thousand dollars, in a hamlet of 2500 people, pleases the inhabitants and promotes the political fortunes of the Congressman who secures it; but it is of no economic benefit. On the contrary, it represents an indefensible waste of public money. The same is true of many river and harbor improvements; the utility of some of which is entirely incommensurate with their cost.

20:—Thus it happens that political expediency and popular demand, rather than economic utility, often determine the extent and application of huge appropriations. Double harm results. Despite the great extent of appropriations for public improvements, much of the money is absorbed, in response

to sectional demands, for economically wasteful local projects, while projects of National benefit and the highest degree of utility are insufficiently provided for.

21:—This is illustrated by the haphazard policy of river and harbor improvement. While upward of \$700,000,000 has been spent for this purpose, it has been spent piecemeal, largely upon unrelated projects, often of strictly local and limited utility. Had it been spent upon a comprehensive and consistent plan, devised for the development of a complete interconnecting National system of waterways, to be improved progressively and with regard to their general utility, the benefit to the Nation would have been much greater. With such a policy we would ultimately have a system of canalized rivers and connected waterways, comparable with those of France and Germany, and of immeasurable importance in our transportation system. Under the policy actually pursued in response to sectional demands, the benefit has been relatively slight, and much of the outlay has been practically wasted.

22:—Another unfortunate result is that the pressing needs of the most important ports of the Nation are relatively neglected, in order that the aggregated demands from other sections may be satisfied. The commerce of the principal ports is a National and not a local concern, but relative utility carries little weight with the majority, who need all the funds in sight to provide for their own local improvements.

#### **EVIL EFFECTS OF INADEQUATE PROVISION FOR BETTERMENTS AND MAINTENANCE.**

23:—A characteristic defect of governmental industrial plants is their low physical efficiency. This is due to the almost invariable unwillingness of appropriating bodies to permit exist-

ing equipment to be discarded until it has become physically unserviceable; and to insufficient outlays for maintenance. A machine is no longer economical when a new and better machine will give a larger output at lesser cost; and sound business practice discards old machinery, even if in perfect physical condition, and substitutes new whenever the resultant saving in operating costs exceeds the interest charges on the additional capital investment required. This is seldom done in governmental plants, and in consequence operating and maintenance costs per unit of production are commonly excessive.

24:—Certain small pumping engines in New York's water supply system illustrate this. The engines in question had been many years in commission and were therefore much inferior, in original potential performance, to more modern types, their local consumption and labor costs per million gallons pumped being relatively very large. In addition, through wear, their actual performance had decreased greatly. The average annual cost, during several years, of repairs to maintain these engines in usable condition, to average about one-half rated service, was about \$20,000. They could have been replaced for less than \$100,000, but the necessary appropriations, frequently urged, were as uniformly denied.

25:—Several hundred municipal lighting plants, which have been installed in various parts of the United States, have failed. The causes have been various. One invariable cause, always present, has been refusal of sufficient appropriations for maintenance and betterments, whereby the plants became inefficient and excessively costly of operation.

26:—No large industrial enterprise can long be kept economically efficient without a continuous addition to the capital

investment, to provide for betterments. Private enterprise provides such new capital because it produces corresponding earning power; but public appropriating bodies can seldom be convinced that economy requires a large additional capital outlay for the partial reconstruction of a plant which was new and fully efficient ten years ago, but which is today economically obsolete. The public almost invariably considers a first large investment as final, and violent public opposition, usually assuming political form, deters legislative bodies from making the additional appropriations which efficiency and economy require.

27:—It is very seldom that public appropriations keep pace with immediate and pressing needs; still more seldom that large present appropriations are made for needs that appear remote, even when present efficiency and future economy are thereby served.

28:—Promptitude in supplying telephone service and economy in construction require the provision of an underground conduit system adequate not only for present needs, but for those of several years to come. It is far cheaper to build a large conduit, much in excess of present needs, than to build a succession of small ones, each of capacity to meet only current demands. Hence, in the City of New York and in other large American cities, the telephone companies have many millions of dollars invested in conduits in anticipation of needs from five to ten years in the future. This policy involves considerable carrying charges on unused equipment, but the saving in construction costs is much greater and the net saving is large. Moreover, this policy of preparedness in advance of demand enables telephone service to be supplied almost instantly. In Japan, where a Government telephone system was installed a few years ago, facilities are supplied piecemeal,

after the demand accrues. Hence excessive cost of installation and excessive delay in meeting the public needs; so that from a year to a year and a half or more elapses before an applicant for a telephone gets it. Similar conditions, although in a lesser degree, prevail in the telephone service of England, France and other foreign countries.

29:—It is unreasonable to assume that legislatures which are dilatory in providing for pressing and immediate needs will authorize large outlays years in advance of present needs, however economically desirable such outlays may be, and however necessary to prompt supplying of service.

30:—In the present restricted field of governmental physical undertakings, insufficient betterment and maintenance outlays are a prolific cause of excessive cost and inefficient service. The harmful effects would be multiplied many fold if extended by governmental intervention into highly complex industrial fields such as railroad or telephone operation.

### **III.—ADMINISTRATIVE INEFFICIENCY OF GOVERNMENTAL MANAGEMENT AND ITS CAUSES.**

31:—In the conduct of large business corporations the chief executives are chosen because of their proved fitness. They are the product of evolution. They commonly begin in the lowest ranks of the service. In subordinate positions, they display more than average ability, zeal and initiative. Because of these qualities they rise above their fellows and are selected for more important positions. Their qualities develop with opportunity. Their best effort is enlisted through self-interest, for there is keen competition for advancement, large opportunity for it, and the best man wins. Rapid promotion comes to the man who proves himself

best qualified to perform the service required. In his upward progress by successive steps the future high official acquires intimate knowledge of every detail of the business, of the best methods, of efficient organization, of the merits and varying capacity of his fellow workers, of discipline, of all the complex matters which an efficient executive must know and control.

32:—Thus exceptional capacity, developed by special training and long and comprehensive experience, is characteristic of the principal executive officials of large industrial corporations; and they are chosen because of that qualification. They have the confidence of their directors, are given prompt and ample support, and have full control over organization, discipline, promotion, and all details of operation. Contrary conditions govern the selection of governmental executives; and the methods employed are peculiarly unsuited to securing officials competent properly to carry on a business undertaking.

#### GOVERNMENTAL METHODS OF SELECTING ADMINISTRATIVE OFFICIALS UNSUITED TO BUSINESS OPERATIONS.

33:—Almost invariably the selection of governmental executives is based upon considerations other than the qualifications indispensable to a good business manager. The method of selection considers popularity and disregards proficiency. It accepts active intelligence as the equivalent of highly specialized training. It assumes that brilliance is synonymous with sound judgment. It assumes that a brilliant lawyer, a high-minded and intellectual idealist, a sincere and vociferous reformer, or a shrewd and able practical politician, is as capable of managing intricate business affairs as a man of long experience, intimate knowledge and highly developed skill in the especial field concerned.

34:—These assumptions are of course in the great majority of cases mistaken. Intellectual brilliance is not a guarantee of sound judgment and in the long run not a dependable substitute for special training and ample experience. Quick understanding is by no means a synonym for organizing capacity. No man, however intellectually able, could successfully organize or operate a great department store without long experience and intimate knowledge of infinite detail. The fact that a political leader has won a large popular following in a radical section, by promoting harmful and even destructive economic legislation, does not qualify him to operate a railroad efficiently.

35:—But under a popular form of government, extensive changes in administrative officials at frequent intervals are inevitable. It is equally inevitable that the political forces which decree the changes shall dominate the selection of the new officials, and that political considerations, and not complete fitness shall, in the main, determine the selections.

36:—We thus commonly have, at the outset, initial unfitness on the part of the business managers selected by Government, in the sense of lack of the especial qualifications required for effective performance of the business function. Even men of much general ability, when injected into a vast and intricate business machine of whose methods and details they are profoundly ignorant, must flounder woefully for a considerable time and depend upon their subordinates. But in government business the principal subordinates also are usually displaced, when the chief is changed, by new and equally untried or unfit men; and until the chief can get his bearings, the machine runs by the inertia of ancient routine. In effect, we have for a time government by Chief Clerks.

37:—It is quite true that men of good capacity, experienced in other fields, may in time “learn their jobs,” and develop into capable business managers; although, at the best, it is unreasonable to assume that relatively brief experience in a new and complex field will develop efficiency equal to that derived from life-long experience. Unfortunatey, the time required fully to learn the job is denied by reason of short tenure of office. Before the process can be completed, a change in officials ensues, and the educational task must be begun anew. Of course, the business drifts while the heads are learning. Any private business would speedily succumb to such conditions.

38:—This phase of the subject was cogently summarized by a Joint Congressional Commission which in 1908 reported upon the “Business Method of the Post Office Department.” The members of the Commission were Senators Penrose, Carter and Clay; Representatives Overstreet, Gardner and Moon. In its report the Commission said:

“For more than one hundred years the great and stupendous business of the Post Office Department has been operated without being overhauled or looked into from the point of critical, expert scrutiny of its business methods \* \* \*. It appears too obvious to require argument that the most efficient service can never be expected as long as the direction of the business is, as at present, intrusted to a Postmaster-General and certain assistants selected without special reference to experience and qualifications and subject to frequent change. Before the Postmaster-General and his assistants can become reasonably familiar with the operations of the service, they are replaced by others, who, in turn, are called upon to resign before they can, in the nature of things, become qualified by knowledge and experience to perform their allotted tasks. Under such a system a large railroad, commercial, or industrial business would inevitably go into bankruptcy, and the Post Office Department has averted that fate only because the United States Treasury has been available to meet deficiencies.”

## DEMORALIZING EFFECT OF FREQUENT CHANGES IN MANAGEMENT.

39:—In industrial affairs frequent changes in management tend seriously to impair the proper co-ordination of the business machine. Each new official is likely to make changes in method and in personnel. Even when wise and desirable, such changes are apt to produce temporary dislocation until operations have become adjusted to the new conditions. If changes are ill-considered, as is certain to be the case when they are made by inexperienced or otherwise unqualified officials, the result is bad co-ordination and impaired efficiency along the whole line. In public affairs the succession of new officials is unending. They are the co-ordinating force of the affairs with which they are charged, and, by reason of their newness, they are usually incompetent effectively to perform the function upon which the efficiency of the organization as a whole depends.

40:—Illy-considered and often harmful changes in methods and personnel are invariable accompaniments of changes in the managing officials in charge of public industrial works. Nearly every new official thinks that extensive reforms in methods and organization are necessary, and is usually right in so thinking. But he generally ignores the fact that intimate knowledge and years of experience are requisite to devise new methods which will actually promote efficiency. The result of his efforts in such case is a new pattern of patchwork and not a new and better machine. He has provided some new cogs which do not gear with old ones; the new cogs make a better show, but the machine does not work any better than before. He makes a show of improvement but fails in its substance, because he does not really know the right thing to do, nor the

right way to do it; and doing the wrong thing slows down the works.

41:—Thus by reason of the changes in method which almost uniformly follow changes in public officials, bad co-ordination, and therefore low efficiency is a distinguishing characteristic of public management, especially in the case of physical works.

42:—Evils of another class result when the new executive, conscious of his at least temporary inability, seeks refuge in inaction, and is content to be a rubber stamp. In that event the actual conduct of affairs falls to a large degree into the hands of minor officials, each of whom is intent upon enlarging the importance of his own bureau, and conducts it so far as possible with jealous disregard of the operations of other bureaus. Differing and sometimes conflicting methods, great inertia, lack of co-ordination and imperfect functioning are the consequence.

The report of the Penrose Commission forcibly shows the evils which have arisen in the Post Office Department from this cause.

#### HAMPERING LIMITATIONS UPON EXECUTIVES.

43:—Even executives of the highest capacity cannot be fully effective under the hampering conditions which prevail in Governmental management, for the reason that they are deprived of necessary discretionary power.

A fundamental theory of our Government is that executive power shall be restricted, in order that the rights and liberties of the people shall not be subverted by abuse of such power. It cannot seriously be questioned that such restriction in Governmental affairs is necessary and wise, but from that very necessity proceeds the inability of Government executives to

act efficiently in industrial undertakings. The public welfare requires an elaborate system of check upon executive action, but the machinery of check in public affairs is always the machinery of inertia and frequently of paralysis.

44:—Congress, having the power to determine the sphere of activity of executive officials, is very tenacious of that power and asserts it with great jealousy. This is well illustrated by the language of Senator Bourne, in the Report of the Bourne Commission on Railway Mail Pay. The Senator said:

“It will be observed that the bill which this Committee recommends for enactment leaves as little as possible to the discretion of the officers of the Post Office Department. We believe this of paramount importance \* \* \*. We believe, therefore, that in the fulfillment of its obligations to the country, it is the duty of Congress, so far as practicable, to enact laws in such form that a minimum amount of discretionary power shall be vested in administrative departments, so that the measure of every man’s rights and duties and responsibilities will be clearly and definitely stated on the pages of our statutes \* \* \*. The greed for power manifested by this recommendation [of the Postmaster-General] is surpassed only by the concentrated egotism which prompted the belief that the Department could exercise such power if granted. Possessed of the power the Post Office Department has requested in the various measures it has proposed and advocated, the Postmaster-General might well exclaim, in the language of a famous European monarch, ‘The State—I am the State!’

“Unless confronted by the record of its recommendations, we would be loath to believe that any administrative department could presume to ask such a delegation of power from an intelligent, self-respecting legislative body, imbued with a fair appreciation of its own functions.”

45:—Aside from the merits of the particular proposition thus stigmatized by an able senator, it is self-evident that the intimate and friendly relations between directorate and executive which are necessary to efficiency cannot exist when Con-

gress resents and withholds powers without which the executive cannot be efficient.

46:—While many executive requests are unreasonable and are properly denied, it is equally true that Congress continually maintains limitations upon executive discretion which make good administration impossible. Its constant aim is, as expressed by Senator Bourne, to leave as little as possible to the discretion of executive officials. It, therefore, completely reverses the methods that are necessary to business efficiency. It prescribes and regulates in minute detail the methods which shall be followed by the executive, and thereby deprives him of necessary discretion. He cannot displace a defective method by a better one by reason of the existence of a law which precludes such action upon his part. He cannot materially change the framework of the organization through which he must work, because the law has prescribed specified divisions, bureaus and sub-divisions which must continue until changed by law. He cannot materially change the personnel of his organization, but, in the main, must take what is handed to him by his predecessor. He cannot create places when required for operating purposes, fix salaries or control promotions except to a limited extent. His powers of discipline are restricted by the Civil Service Laws and relatively inefficient employees are, therefore, safe unless their transgression is flagrant.

47:—In industrial undertakings, conditions are constantly changing and the methods of management must be quickly adapted to meet the changed conditions. It is necessary, therefore, that the executive have large discretion as to methods, personnel, choice of assistants, salaries and promotions. The limitations which Congress imposes deny all these to the executive. The result is rigidity of method which tends to ossification, whereas elasticity is requisite.

48:—The strict inhibition by Congress of any outlays not specifically authorized by itself is particularly obstructive in many minor but necessary details of administration. On this point we quote from the documents of the Penrose Commission:

“The system of appropriations which is admittedly necessary in the Government service is another feature in which the Post Office differs from a private corporation. In the latter appropriations are made for specific purposes in the shape of authorities given by the highest officials for current expenditures, and if at any time these appropriations are found to be insufficient or if, for any reason, it is deemed advisable to increase the expenditure, this can be done immediately, and even if the amount authorized be exceeded, provided that proper reasons are given, no exception is taken and no harm done.

“In the case of appropriations by Congress, however, it is entirely different. There are strict penalties for exceeding an appropriation \* \* \*. In the course of our investigation we have found many instances in which the work in certain divisions has had absolutely to stop before the end of the fiscal year because the appropriations had become exhausted. In Cincinnati, for example, the printing plant was lying idle for weeks, all the salaries of the printers continuing as usual, owing to the appropriations for paper being exhausted. Meantime, the printing necessary was done by an outside printer and paid for under some other appropriation.

“The traveling allowances of the officials of the Railway Mail Service, whose duties consisted of personal inspection of the efficiency and needs of the service, having reached the limit set by the appropriation, these men were compelled to allow their work to lapse for several weeks before the close of the fiscal year. It is obvious that, under such conditions, the service must suffer \* \* \*. There is a lamentable lack of labor-saving devices practically throughout the whole Department and Service, even for such an elementary machine as a typewriter. We are informed that there are hundreds of applications on file which the department has been quite unable to fill. Of the more complicated machines, such as arithmometers, book typewriters and calculating machines, there are few in use and even in the field Post Offices such scales as are provided for the special weighing of mails now in progress are of a very inferior grade and from the information we have gathered it would appear

that, with few exceptions, there are no mechanical conveying devices in any office for expeditiously handling and weighing the mails.''

It is obvious that under such hampering conditions as have been recited, efficiency on the part of any executive is greatly reduced.

49.—Another contributing cause to executive inefficiency is the prolonged delay of Congress in determining important questions of policy, and the delaying or withholding of indispensable appropriations. This phase of the subject has been discussed in Paragraphs 13, 14 and 23, and need not be repeated.

#### LACK OF SELF-INTEREST AS AN INCENTIVE.

50:—The motive of self-interest is dominant in all industrial enterprises. It induces the investment of capital therein; it permeates the directorate and enlists the careful attention and best energies of its members; it operates powerfully to develop executive officials of the highest ability and to secure the assiduous devotion of that ability to the efficient and profitable management of the properties. It secures similar zeal upon the part of all minor officials, and induces faithful and diligent service by the rank and file of employees.

Throughout the entire service of an industrial corporation employing thousands of men, practically every one will be stimulated by the desire to better his condition through faithful service and the free opportunity afforded him by industrial organizations.

51:—The incentive of self-interest proceeds from the system of promotion which prevails in private employment; namely, free selection by the higher officials from the ranks of their respective subordinates, of those who prove them-

selves best qualified for more important duties. Efficiency and economic value are the tests. Under such a system the opportunities are numerous; the rewards in the form of salary increase are substantial; and the best energies of every worker are enlisted to promote the interests of the business.

52:—Contrary conditions prevail in Governmental service. Formerly, when the executive was given a free hand in the matter of selection and promotion, the great body of employees was selected almost entirely without regard to fitness and with a view to political considerations. The number of employees was constantly swelled and invariably far exceeded the number required for the functions to be performed. Promotions were made upon a basis of favoritism and political usefulness, and often regardless of efficiency. The wastefulness was extreme and the morale of the workers was completely demoralized. Efficient and faithful men were discouraged by being passed over, while worthless fellow employees were promoted.

53:—To prevent these political abuses the Civil Service Laws were enacted to regulate the conditions of selection and promotion. These laws have succeeded in greatly reducing the political abuses indicated, but they have caused another class of evils. While they have given security of tenure to employees, they tend to retain in place the relatively inefficient as well as the deserving, and they deprive the executive of the power of choosing for promotion the men best qualified for more important duties. The higher places, moreover, not being under the operation of the Civil Service Laws, are still open to appointments by favoritism and political influence, and the great stimulus of opportunity to fill these higher places is thereby taken away from the rank and file, who are reduced to discouragement and to the performance of duty in a per-

functory way, by reason of the absence of an incentive, of which they are deprived by existing conditions.

54:—The Twenty-third Report of the Civil Service Commission says:—

“The great defect in the Federal Service today is the lack of opportunity for ambitious, well-educated young men. All of the higher positions are outside of the competitive classified service and no system has been established by which those who have distinguished themselves in the service can be promoted to the more important offices and at the same time enjoy reasonable security of tenure. There is not sufficient inducement for the most capable men to enter the examinations, as they can do better by seeking employment in large corporations, trusts, and other institutions where they can in time command much higher salaries than they can ever hope to secure in the Government service \* \* \*. The Government cannot hope to compete with private employers unless it pays salaries that measure up fairly well to the standard of private business.”

55:—The absence of self-interest as an incentive degrades the standards of personal efficiency in the Governmental service. It is difficult to secure in the higher administrative positions the services of men of first-class specialized ability, by reason of the excessively low salaries paid by the Government as compared with those paid by large corporations; by reason of the insecurity of tenure; and the hampering conditions already explained, which prevent able men from being fully effective.

56:—In the lower ranks, while the employees are commonly paid more than similar work commands in private enterprises, there is small opportunity to rise and little or no reward for exceptional ability. Under these conditions, the best and most ambitious men eventually leave the Government employ, and thereby reduce the general level of capacity of the entire body of employees and place it upon a much lower plane than prevails in private business.

## LACK OF STANDARDS OF EFFICIENCY AND WASTEFULNESS IMPOSED BY LAW.

57:—A high standard of efficiency on the part of every employee is a chief concern in all private business. In manufacturing undertakings, especially, it is vital to continued existence, for competition would soon wipe out any corporation whose labor costs were excessive. To control this important element, tasks are minutely sub-divided and careful records are kept of the time required for and the output of every separate operation. The extent of the work which should be performed by every employee is thus developed and all employees are held to the fixed standards. Labor costs are thus held to a minimum and the due productivity of every employee assured.

58:—These industrial methods are seldom employed in Governmental work. The cost of caring for public buildings is commonly more than twice the cost in the case of private buildings. When streets are repaired by Government labor, the cost is usually excessively great. In public offices, the cost of clerical services, when tested by the work performed, is usually several times that of similar services in the case of large corporations.

59:—A striking illustration of the difference between Governmental and private methods in the matter of efficiency is supplied by the Tavenner Bill passed by the last Congress, which forbids the use in Government offices of means for providing standards of efficiency and thereby exacting from employees a fair measure of service. A low rate of productivity of course results from the conditions outlined above.

60:—With this is combined a further element of wastefulness resulting, in several states, from legislation affecting the

rate of wages to be paid in certain public employments. In the State of New York workmen employed upon public works, whether directly in public employ or in the employ of contractors, must be paid the so-called current rate of wages. The rate so fixed is, in fact, commonly much in excess of the true rate of wages prevailing. In some states the materials used in public works must be locally produced, the bringing of better and cheaper material from other States thereby being precluded. In some instances, this limitation works directly for the benefit of a very small class of producers and naturally results in excessive cost.

61:—The standards of efficiency of Government employment are materially lower than those of private employment. The rate of wages for minor employees is materially greater; the hours of labor are materially shorter. These factors combined result in excessive labor costs for all Government undertakings. If the public utilities of the country are taken over by the Government, there will be somewhat more than three million government employees. Let this number be multiplied by the difference between the labor costs of Government work and private work, and a formidable aggregate increase in labor costs would result, probably fully equal to the profits now accruing from private investments in public utilities.

#### **IV:—POLITICAL AND FINANCIAL CONSIDERATIONS.**

62:—There are at present approximately 2,000,000 railway employees in the United States. Other public utilities, including telephones, telegraphs, electric lighting plants, urban and inter-urban electric railways, other street railways, water transportation lines and express service, will raise the aggre-

gate number of employees who would ultimately enter some form of Governmental employ under Government operation of public utilities to about 3,000,000 persons.

63:—No proper consideration of this subject can ignore the political dangers which might readily arise from this source. Senator Bourne points out that in the last ten presidential elections the President has been elected by a plurality varying from 7000 plus to a little more than 2,500,000. A body of government employees numbering 3,000,000 intent upon better pay, less service, shorter hours, and other personal advantages, might readily hold the balance of power between the principal opposing political parties, and make the choice of a President and the policies and methods of government dependent upon concession of demands made by an organization of Government employees. So numerous a body of voters, animated by a common purpose, might well become a “third party,” frequently holding the balance of power and making the direct purposes of Government and the welfare of the whole people subordinate to their own selfish purposes—a Pretorian guard, choosing the emperor and dictating all the affairs of the empire.

64:—The outstanding securities of the railroads, together with their unfunded debt, is now in excess of \$20,000,000,000. The aggregate securities and unfunded debt of other public utility corporations is approximately \$8,000,000,000, a total of \$28,000,000,000 of invested capital represented by stocks and bonds, which would have to be refunded and substituted by National, State or Municipal securities if public utilities be governmentalized.

65:—One argument invariably advanced in support of Government ownership and operation is the saving in interest

charges due to the superior credit of governments. It may be assumed, therefore, that the outstanding corporation securities which now return interest or dividends at the rate of from 5% to 8% would be substituted by Government bonds carrying interest at 3%.

66:—No refunding operation equal in extent and danger to this has ever been undertaken. To suddenly reduce the earning power of \$28,000,000,000 of capital by more than one-half would probably produce a financial cataclysm, and would certainly profoundly disturb the entire financial and economic structure of the country. All the enormous investments of savings banks and life insurance companies would be rendered either little profitable or unsafe. The ordinary investment channels which assure a combination of safety with a moderate return of profit would be in large degree closed and, as is always the case when great volumes of free capital are seeking profitable use, speculative investment in unsound companies and ultimate loss would be greatly promoted. Possibly some safe means of effecting the enormous refunding operation indicated might be found, but the dangers attendant upon it should not be overlooked.

67:—The railroads of the country now contribute to the cost of government more than \$150,000,000 each year in the form of taxes. The taxes paid by other public utilities would probably increase the total to over \$200,000,000. The funds derived from these taxes accrue to the several states, municipalities, or other political divisions where the property is located. In the event that these utilities become the property of the Federal Government, they would no longer be subject to taxation and the several states, and their inferior sub-divisions, would thereby be deprived of a principal source of revenue from which to meet the expenses of government. One

result, therefore, of government ownership of public utilities would be that other forms of property would have to bear a materially increased burden of taxation.

## V:—SUMMARY AND CONCLUSION.

68:—The defects of Government procedure in economic undertakings have been outlined. Those defects are ineradicable because they are rooted in our political institutions. The principles that govern political action and those that govern economic action are fundamentally different and cannot be reconciled.

69:—The purposes intended and the methods by which they are accomplished are inherently different and in many respects antagonistic. Political action takes concrete form only after a long period of deliberation and discussion and the processes of legislative bodies are, therefore, almost invariably slow. The application of such methods of long delay to the conduct of economic affairs is destructive and any business conducted on such principles would speedily die.

70:—In political affairs the welfare of the people requires that as little power as possible be granted to the executive. The proper conduct of economic affairs requires that very large powers and, in certain particulars, unhampered discretion be given the executive. In private affairs the powerful motive of self-interest is always present and exerts a potent influence upon all concerned therein. This motive has but a limited existence in public affairs and where it exists is often opposed to the public welfare.

71:—In the management of industrial undertakings the legislative branch of governments commonly fails to provide

funds when needed, is vacillating and dilatory in deciding questions of policy, retains to itself powers without which the executive cannot effectively act, and does not and cannot maintain with the executive the close relations essential to good management, nor afford the support without which the executive is incapable of full effectiveness.

72:—In the executive branch inexperience, and therefore at least temporary incapacity, is the rule as to the chief officials. When capacity exists or has been developed by experience, its exercise is largely precluded by frequent change of officials and conditions of law imposed by Congress,—conditions which preclude proper financing, capable executive management and effective co-ordination. The highest degree of efficiency and economy is therefore made impossible, not because of unintelligence or improper purpose either on the part of Congress, the executive officials, or the members of the staff, but by reason of the fact that the harmful conditions indicated cannot be escaped when a form of procedure suitable only to political action is applied to industrial undertakings.

73:—The case of the Post Office Department well illustrates this proposition. Every Postmaster General during more than a generation has complained with more or less bitterness of the defective procedure prevailing in that Department, and has sought with more or less earnestness and ability to effect a reorganization. In 1882, the Postmaster General in his annual report strongly represented to Congress the wastefulness arising from the manner, imposed by law, of making allowances to postmasters. He showed that the distribution of allowances amounting to almost \$5,000,000 was wholly within the discretion of a fourth class clerk in the office of the First Assistant. He also incidentally pointed out that the salaries paid to a large class of these postmasters were mere

sinecures for which no service was rendered except the signing of official papers. Twenty-five years after Postmaster General Howe had shown this specific evil, the same conditions existed, with the exception that the fourth class clerk in question controlled the allotment of over \$25,000,000.

74:—The affairs of the Post Office have been subjected within recent years to the scrutiny of two exceptionally able Congressional commissions, which have scathingly criticised the methods of that Department and recommended extensive changes. The changes have not been made, principally because political and not economic considerations have dominated the administration of the Post Office Department. In view of the failure of attempts adequately to reform the methods of the most important of Government utilities, it may fairly be concluded that the methods which have hitherto dominated the Government management of economic affairs will continue to dominate them in the future. In conclusion, attention is asked to the situation which would ensue upon the application of such methods to the Government management of railroads.

75:—In the fiscal year ending June 30, 1914, the combined expense outlays of the railroads of the country were over \$2,214,000,000. The investment outlays were over \$637,000,000,—the latter sum probably not more than one-quarter of the annual amount reasonably necessary to provide transportation facilities adequate to the Nation's needs.

76:—In the event of Government operation, on the basis of present outlays, the expenditure of not less than three billions of dollars annually, for railroad purposes alone, would be controlled and directed by governmental agencies. It is beyond the bounds of reasonable probability that expenditures of such large extent can be so apportioned, through the

agencies necessary under a democratic form of government, as properly to provide for all the infinite needs of a vast and extraordinarily complex organization, whose ability to serve depends upon sufficient and continuous financial sustenance for all its multitude of parts.

77:—It is certain that an annual railroad budget of \$3,000,-000,000 or more would be fiercely assailed both in and out of Congress. It is certain that in some years a demand for economy would cause it to be ruthlessly cut, that funds absolutely necessary for even moderate efficiency would be withheld, and the entire organization thereby hopelessly deranged.

78:—The distribution of outlays would be governed, not by economic, but by political expediency, and by sectional demands of an extent and force far exceeding any hitherto known. The competition of sections for public buildings and for river improvement and the uneconomic use of public monies resulting therefrom, huge as it is, would be trivial compared with the competition for local railroad improvements. That not needed would often be done; that urgently needed would often *not* be done. The funds spent would to considerable degree be economically wasted; and in place of an organism with all its parts properly correlated, and therefore capable of high efficiency at a minimum cost, we should have an organism so badly correlated and so defective in all its parts that its efficiency would be very low and the cost of operation excessive.

79:—The preceding survey of the field thus shows in the governmental operation of public utilities defects which are insuperable obstacles to economic efficiency. Those defects proceed from and are rooted in the political principles upon which our form of Government is based. The American people be-

lieve that nothing should be done except that explicitly authorized by the representatives of the people. They believe that liberty and civil rights will be subverted unless public officials be frequently changed. They believe that the powers of such officials should be severely limited, that their discretion should be restricted to the uttermost, that they should do nothing until the Legislature shall have given its assent and prescribed the manner of doing.

So:—But the methods which are the inescapable result of these principles are repugnant to and destructive of good management of business affairs. The methods of our Government proceeding as they do from political principles profoundly rooted in the Nation's convictions, although they may be somewhat modified cannot be essentially changed. These methods, when applied to the field of economics are deadly blights. To subject to their demoralizing and destructive influence such vital elements of the National industrial life as the railroad, telephone and telegraph systems of the country, would almost certainly impair to an extreme degree the usefulness of those invaluable public instrumentalities, and prove an immeasurable misfortune.

F. B. DEBERARD.

*Director of Research,  
Merchants' Ass'n. of New York.*

## III: GOVERNMENT REGULATION OF TRANSPORTATION

---

### I:—EFFICIENCY OF THE VEHICLES OF TRANSPORTATION VITAL TO THE NATION.

PRESIDENT WILSON recently wrote:

“The interest of the producer, the shipper, the merchant, the investor, the financier and the whole public in the proper maintenance and complete efficiency of the railways is too manifest. They are indispensable to our whole economic life, and railway securities are at the very heart of most investments, large and small, public and private, by individuals and by institutions.”

The intent of public regulation is to secure the complete efficiency which President Wilson has described, to protect the public against abuse and to assure to the public reasonable rates of charge for the service vital to it.

The need of such regulation is unquestioned. When such regulation by public authority was lacking, the railroads were assumed to be private business undertakings in the management of which the public had no right to a voice. Their operation was marked by financial exploitation, excessive rates, discrimination, rebates, favoritism, and insufficient service. The former doctrine of private control has, however, been fully exploded. Railroads are now unreservedly con-

ceded to be instrumentalities of the public, existing by virtue of public authority and therefore subject to whatever degree of public control is required to enable or compel them fully to serve the public needs and to protect the public rights.

The right of public control has been asserted and extensively exercised. Under such control the characteristic abuses of the past, against which public indignation was justly directed have been in large part abolished. But unfortunately much of the legislation hitherto directed against railroads has been in response to popular demand expressive of popular indignation. It has been in the nature of reprisals for past misdeeds rather than in the nature of wise remedies for economic evils. With much that is sound and useful has been combined much that is unsound and harmful. The power of regulation has been exercised through a multiplicity of independent authorities, operating without co-ordination, with differing and sometimes opposing methods. By reason of this unco-ordinated and multiple regulation through independent bodies, has arisen conditions which tend seriously to impair the power of the railroads to render efficient service, and which therefore tend to defeat the main purpose of regulation.

## II:—WHERE THE POWER OF REGULATION RESIDES.

**R**AILROADS are now subject to regulation by the national authority and by each state in which their lines are located. Hence has arisen a diversity of conflicting requirements.

Besides the laws of Congress, which are of general application, there are many hundred laws passed by the several states, many of which are inconsistent with the Federal Laws

and with the laws of other states, and while they are of local application, they tend in large degree to nullify the intent of the Federal Laws and create conditions which either cannot be uniformly complied with or, as an alternative, involve extreme and wasteful expense.

This conflict arises from the assumption that each state may rightfully, within its own borders, regulate commerce and its vehicles. This is true only so long as Congress refrains from asserting and exercising whatever superior powers of regulation it possesses.

The power of Congress within its constitutional limits, is supreme whenever asserted and to the extent of its assertion. When, therefore, Congress undertakes the regulation of railroads as carriers of interstate commerce, the inferior powers of the states, in so far as they impede or obstruct the national will as constitutionally expressed by Congress, must yield.

The Constitution provides that—

“The Congress shall have power:

(3) To regulate commerce with foreign nations and among the several states.”

Congress has already asserted and exercised, in part, its power of regulating interstate commerce and has construed it to comprehend the regulation of the agencies and the instruments by means of which such commerce is carried. The entire fabric of the “Act to Regulate Commerce” is based upon this interpretation. It assumes that whatever is a necessary instrument in the movement of commerce between the states becomes, from that fact, subject to National regulation.

But all railroads, whether extending through two or more states, or solely within a single state, are necessary instruments

of interstate commerce. Even in the case of strictly intra-state lines, much, and often most, of their traffic consists of commodities produced in and shipped by consignors in other states, to local consignees, and vice versa.

Moreover, all railroads carry local commerce, strictly within the limits of a single state. Thus every railroad has a dual capacity; as a carrier of interstate commerce, which function subjects it to National regulation; and as a carrier of intra-state commerce, which subjects it to State regulation. Thus, a condition of dual regulation of the same vehicle results.

From an economic standpoint, this dual regulation is detrimental. Sole regulation by National authority would in many respects be economically beneficial. But whether Congress has power under the Constitution to assume sole regulatory control of all railroads, on the ground that they are all necessary vehicles of interstate commerce, and that State regulation interferes with and impairs their efficiency as such interstate vehicles, presents a very difficult and perplexing constitutional question.

This argument does not undertake to discuss that legal question, but confines itself to showing the evil economic effects which result from dual or multiple regulation, and to advocating sole Federal control as a remedy. If Congress has, under the existing constitutional provisions, power to assume sole regulation of all railroads, the full exercise of that power would be highly beneficial, and if Congressional power is now lacking it might well be conferred by a suitable amendment to the Constitution.

### III.—INCONSISTENCIES AND HARMFUL EFFECT OF MULTIPLE REGULATION.

**I**T is self-evident that great diversity must ensue from independent and unco-ordinated action by Congress and forty-eight legislatures, and the commissions through which their mandates are given effect. It is equally evident that when a single organism is subject to numerous independent authorities and made the object of varied and conflicting orders, the proper workings of that organism must be seriously impaired and its functions badly performed. A condition of great confusion and low efficiency must necessarily result.

There can be no reasonable doubt that Congress was given power to regulate commerce between the states in order that no state should for its own benefit obstruct or impede the commerce of other states.

But the regulatory powers over railroads now exercised by the various states produce such obstruction. It is not possible for any state to undertake the regulation, within its borders, of any railroad (except as to limited police matters), without producing effects reaching far beyond the borders of the state and affecting the movement of commerce, not only within the state but in far distant parts of the country.

This condition already exists because of the regulative laws of several of the southwestern states. It is clearly the intent of the Constitution that there shall be a free and unimpeded movement of commodities throughout the boundaries of the nation. This movement is precluded by the laws of Texas, Alabama, Arkansas, Mississippi and other states. In some of these states freight charges have been fixed, either by legislatures or commissions, with a view to excluding, by means of discriminatory local rates, the products of other states, in order that, by reason of an advantage in freight rates thus

secured, local merchants should be relieved from the competition of those located without the state.

In these cases rates applying to local traffic have been fixed by law so low as just to escape confiscation, in order that commodities moving solely within the state shall be subjected to a materially lesser freight burden than is borne by commodities coming from without the state. So we have a condition expressly designed to obstruct the free movement of commodities—a condition under which, by state authority, barriers against such free movement are raised.

In numerous states large wasteful expenditures are enforced by law. The train-crew laws, adopted by twenty, but rejected by twenty-one states, afford an example. The purpose of these laws is solely the enforced employment of more men. They serve no useful purpose whatever, but impose upon the railroads a heavy burden of wasteful expense, and divert the outlays from useful channels in which they would benefit the public. In 1914 the "full train-crew" laws cost the Pennsylvania Railroad \$850,000. The aggregate expense imposed by these laws upon 166 railroads was over \$4,050,000, equal to a 5 per cent. charge upon \$80,000,000.

Reduction in the length of freight trains is now strongly urged in many states, although not yet adopted by any. Such reduction would not only greatly increase operating costs, but would nullify the utility of huge investments hitherto made for the express purpose of promoting the handling of large trains—the most important factor in railroad operating economy and in its influence upon low freight rates.

Fourteen states have dissimilar safety appliance laws. Fifteen states require a minimum daily movement for freight cars in transit, regardless of the almost insuperable difficulties imposed by conditions which can only be removed by large investments of new capital. Some of these states require a

minimum movement of 50 miles per day—about twice the average for the whole country. In some cases it is sought to favor local traffic by imposing excessive penalties, one state fixing a penalty for delay of \$10 per hour. Twenty-eight states have non-uniform head-light requirements.

Various states impose penalties for failure to provide freight cars upon demand. The penalty in Indiana is \$1 per day; in North Dakota \$2; in Kansas and North Carolina \$5. The effect of the variance in penalties is that the state where the largest penalty prevails gets the cars, while its neighboring states are discriminated against, and their car shortage made more acute.

By reason of the multiplication of regulatory bodies, the railroads of the country are now required annually to make over two million reports of various kinds. The form of these reports varies by reason of differing requirements of the several states. The expense of compliance is enormous. The cost of the separate investigations ordered by the different states is also very great. Numerous other local requirements involving large cost are in effect.

The aggregate wasteful expense is very great and it might be in large degree avoided were it not for the separate operation of state legislatures and commissions. In consequence of such legislation regulating operation, 116 companies expended upwards of \$28,700,000 in 1914, little of which was for beneficial purposes. This sum, if saved, would have paid the interest upon \$574,000,000 which could have been devoted by the companies to improvements sorely needed to increase their efficiency.

The effect of discriminatory local rates, and of wasteful outlays imposed by local laws is not local. In such cases the proper revenues, necessary to the efficiency of the railroad as a whole, are depleted, thereby either depriving the residents

of other States of the degree of service to which they are entitled, or, as an alternative, compelling them to bear an undue share of the cost of properly maintaining and operating the road.

It is obvious, therefore, that the present machinery of regulation is seriously defective in that it produces conditions of great disparity between different sections of the country, creates barriers against the free movement of commerce instead of promoting such movement, and decreases the efficiency of railroads as a whole.

State regulation, by hampering the instruments of commerce, has potentiality to nullify the intent of the Constitution that commerce between the states should be untrammelled by state action. It prevents effective and consistent operation of railroads and thereby seriously impairs their efficiency. Railroads are the highways of the nation, and as such, they should not be restricted in their effectiveness, impeded or obstructed by local authorities. The national welfare requires that railroad regulation be based upon national, and not local, considerations; that it be coherent and consistent; that it be not punitive of past misdeeds; and that it be uniformly directed throughout the bounds of the nation, to promoting the efficient service which is the people's right and which can only be provided by unification of regulation and by conservation of railroad resources.

#### IV:—EFFECT OF MULTIPLE REGULATION UPON RAILROAD CREDIT.

**T**HE credit of railroads at the present time is in a very depressed condition. During several years past, the investment, without security, of capital in railroad undertakings has steadily declined until at present it has almost

ceased. The public has reached the point where it is distrustful of the safety of investments in the stocks of railroad companies. Hence the latter are now forced to rely almost wholly for their financing upon the proceeds of bond issues; that is to say, upon loans secured by mortgage upon existing properties. It is obvious that this source of new capital cannot much longer be depended upon, for the reason that the security available for new bond issues will be subordinated to existing loans, and therefore eventually cease to be safe.

The reports of the Interstate Commerce Commission show, during a long series of years a gradual and practically constant decline in the net earnings of railroads. The Commission, in its decision of the recent "Five Per Cent. Advance" case declared that the net operating income of the railroads "is smaller than is demanded in the interest of both the general public and the railroads \* \* \*. Their net operating income is insufficient and should be increased."

During the eight years from June 30, 1907 to June 30, 1915, the railroads expended an annual average of \$600,000,000 for improvements and enlarged facilities. This new capital added nothing to the net revenues. On the contrary, despite a continuous and large increase in tonnage and traffic mileage, the net revenues in 1915 were some \$21,000,000 less than in 1907. That is to say, the recent capital investments in railroads, which are approximately 25 per cent. of the entire amount, are not self-sustaining, but impose an additional charge upon the earnings of previous investments.

The unwillingness of investors to place their money in railroad enterprises without security (that is, to purchase new issues of railroad stocks) is due mainly to the gradual but almost constant decline in net earnings which, in turn, is due to two causes:

- (a) Reduction of rates imposed piecemeal through the operations of the Interstate Commerce Commission and the independent commissions and legislatures of practically all the states. The aggregate result of rate reduction through these several channels is very great.
- (b) A heavy increase in operating costs arising not only from the general increase in the cost of materials and labor, but also from state laws which make mandatory large expenditures for numerous diverse purposes, all of which are economically unproductive and some of which are wholly wasteful. The ultimate effect of all these laws is to add greatly to the cost of operation and in some respects to impair rather than to increase efficiency.

The constant trend, therefore, of regulation has been in the direction of impairment of railroad net revenues, until their managers can no longer obtain from the public the funds requisite properly to provide for the growing needs of the country's commerce. The result is already strongly evident in the present marked deficiency of railroad facilities, which must inevitably continue and increase until regulation is directed toward placing and keeping the railroads upon a sound economic basis. That can be effected only by lifting the burden of wasteful outlay now imposed by state regulation, and by adjusting rates with reference to the cost of service instead of with reference to popular demand.

## V:--TRANSPORTATION NEEDS OF THE PUBLIC.

THE railroads of the country, as a whole, are at the present time materially below suitable standards of efficiency. The impairment of their credit during recent years has been such that they have been unable to command the capital needed for the betterments necessary for properly moving the country's commerce. The result of insufficient capital outlays has been strikingly shown by the recent and still existing congestion in traffic movement, assumed to be due, in large degree, to the abnormal movement of commodities incident to the war in Europe, but due, in addition, to the inability of existing facilities to handle promptly the normal traffic movement of the country when at its seasonal maximum.

Congestion of traffic has been a regular occurrence during crop moving seasons for several years past, and in case of unusual business activity the movement of traffic is immediately impeded. The fact is that the investments of the railroads in the betterments needed for prompt traffic movement have been proportionately much less than the increase in the volume of traffic required to be moved. There has been especial deficiency in the matter of provision of adequate terminals. Speaking broadly and with a few exceptions, the terminal facilities of the railroads of this country are completely outgrown. They were planned in a haphazard way in earlier days when the requisites for terminals were not fully appreciated, and when the importance of providing for future growth was not obvious. In consequence, there is scarcely an existing railroad which has terminals of such design and of such extent as are indispensable to the rapid handling of the freight service. To provide such suitable terminals implies the purchase in every city of large tracts of exceedingly

valuable real estate, the practical reconstruction of existing trackage and the adoption of modernized plans which will permit the rapid despatch and unloading of freight trains. It is commonly assumed that the slow movement of freight is mainly due to the lack of cars. This is only partly true. The main impediment is the lack of adequate terminals without which quick movement is impossible, and which lack in itself makes necessary a much larger equipment of rolling stock than would otherwise be required. The insufficiency of these pressingly needed facilities, the absence of which inflicts severe harm upon the business community, is due primarily to the declining credit of the railroads, by reason of which they cannot command the capital necessary to reasonable efficiency in this respect.

It has already been pointed out that this condition of insufficient credit, and therefore of insufficient facilities, is largely due to the increased cost of operation and reduced revenues resulting, to a considerable degree, from the mandates of forty-eight legislatures or commissions operating independently. The remedy for it is the substitution for the present numerous diverse regulatory bodies, whose viewpoint is purely local, of a national tribunal whose breadth and ability shall qualify it to devise such methods of regulation as shall conserve the efficiency of the railroads instead of impairing it; and which shall in all things determine its action upon the broad considerations of national welfare rather than upon the narrow considerations of local benefits.

## VI.—REGULATION OF ISSUANCE OF SECURITIES.

**I**T is doubtless desirable and often necessary that railroads should not possess the power to issue securities until the purpose to which the funds are to be applied are shown to be necessary and proper purposes. Flagrant abuses were com-

mon in the past by reason of unrestricted power in this respect, and to this cause is traceable much of the over-stringent legislation that now exists.

It is wise and reasonable that the public should be assured through its proper agents that the funds derived from the sale of bonds and stocks are properly necessary for the efficient conduct of the railroads, and that they are applied to the purposes for which they were issued; but it is wholly unnecessary in the public interest that this process of scrutiny be indefinitely extended and that it be exercised by several states with reference to the same issue of securities; that diverse regulations affecting such issue be prescribed by the different states; and that the refusal of one state to approve should be permitted to nullify the approval of other states, and thereby prevent the railroad from obtaining the funds genuinely necessary to its proper purpose.

Such a condition, however, exists, and it is further aggravated by the requirement which exists in some states that at least a portion of the funds obtained from any issue of stocks and bonds shall be expended within the state, irrespective of the locality where the application should properly be made.

Other states see in the power over issuance of securities an opportunity for exacting from railroads a heavy tax as a condition upon which the funds may be obtained. The New York Central Railroad, having but a few miles of line within the limits of the State of Illinois, was recently compelled to pay to that state \$600,000 for the privilege of issuing bonds to provide funds for betterments located wholly within other states. It need scarcely be said that this is an abuse of the taxing power detrimental to the public of the entire country, by reason of the effect of needless and wasteful outlays upon the general efficiency of the property so burdened.

In respect of control of securities, adequate investigation by a single well-qualified commission will suffice to protect every public interest and will promote the welfare of both the public and the railroads.

## VII.—CENTRALIZED REGULATION DESIRABLE.

**M**ORE than 80 per cent. of the nation's rail traffic is interstate, and therefore of National concern. The railroads by means of which this traffic is carried are the highways of commerce. Their high efficiency is of immeasurable National importance. It is vital to the general welfare that their efficiency be promoted and expanded; that whatever regulation be applied to them have in view the welfare of the Nation as a whole; that it be just, consistent and economically helpful.

But nevertheless, by the absence of single centralized control, the regulation of the Nation's highways has fallen into the control of local authorities; and those National highways are regulated for local benefit as though they were local affairs. Hence has arisen a body of unrelated, inconsistent and obstructive local regulation, disregardful of the National character of the railroads, and which seriously impairs their power properly to perform their National function.

The present chaotic condition is exceedingly detrimental. Single regulation by National authority would abolish the evils arising from multiple control. The business sentiment of the country is generally favorable to the abolition of diverse state regulation and the substitution of national authority. Intelligent business men do not wish regulation of railroads to take the form of reprisals for past wrongs, concessions to passing popular prejudice nor financial discriminations against part of the country for the benefit of other parts.

They wish rates as low as reasonably possible, but they clearly understand that efficiency of service is more important than low rates, and they do not wish the railroads starved and thus incapacitated from giving good service.

The principles of business efficiency are already applied in a remarkable degree to the management of railroads. The abuses against which the public rebelled years ago are practically eliminated. The necessity for punitive legislation has practically passed away. The present need, therefore, is for regulation which shall carefully eliminate sectional and political motives; which shall proceed along judicial lines; which shall be determined solely upon sound economic grounds; and which shall give full regard to the need for conserving the instrumentalities of commerce as a necessary means for promoting the welfare of the whole people.

Adequate increase of the number of members and the powers of the Interstate Commerce Commission and the taking over by the Federal government of the sole control of regulation of railroads would be a wise and beneficial measure and tend greatly to improve the railroad system of the entire country.

F. B. DEBERARD.

*Director of Research,  
The Merchants' Ass'n. of New York.*

